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SUBJECT: GOJ OFFICIAL UPBEAT ON PRIVATIZATION, PESSIMISTIC
ON COUNTRY'S FINANCES

REF: 06 AMMAN 8241

¶1. (SBU) SUMMARY: The Chairman of Jordan's Executive Privatization Commission (EPC), former Finance Minister Mohammed Abu Hammour, painted an optimistic view of the progress of privatization in Jordan. After a record year for privatization in 2006, 2007 should also register major progress, including sale of Royal Jordanian Airlines. Abu Hammour was very concerned about the growing current account and budget deficits, and the country's debt picture. END SUMMARY.

ANOTHER BANNER YEAR FOR PRIVATIZATION AHEAD

¶2. (SBU) In a January 28 meeting with the Ambassador, EPC Chairman Abu Hammour agreed that 2006 had been a great year for privatizations in Jordan (reftel). However, he expects 2007 to be great too. Partial privatization of the national airline, Royal Jordanian, will be accompanied by private sector opportunities in a BOT to expand Queen Alia International Airport. There will be further government tenders for an Amman-Zarqa light railway, a replacement for Jordan's sole oil refinery and for a Saudi-Jordan water pipeline. The winners for Queen Alia and Zarqa should be announced in April.

¶3. (SBU) Abu Hammour noted that he had had to defend a proposed internal rate of return (IRR) of 15-18% by the bidders on some of these projects to conservatives in the cabinet fearful of "losing" Jordan's patrimony. He argued that this IRR was necessary to reward investors for the risks taken and is typical for such projects worldwide. He added that if the government had to pay for all of the upcoming projects, it would raise the country's debt and affect the Moody's and S&P ratings of the country's financial health.

¶4. (SBU) Abu Hammour expects a total of $6 billion in privatizations and private sector partnerships over the coming years, including those mentioned above. Some of the other projects include state-owned power companies and independent power projects. He expects these projects to generate many new jobs, noting that the liberalization of the telecoms sector had created at least 7,000 new jobs in Jordan.

WORRIED ABOUT FINANCIAL TRENDS

¶5. (SBU) Abu Hammour, a former Finance Minister known as a fiscal conservative, expressed concerns about the current state of Jordan's economy. He was particularly worried by the rising budget and current account deficits and the

prospects for the country's debt burden. "Things are not moving in the right direction," he lamented. He said the budget deficit projected for the 2007 budget is the highest in that last four or five years (septel will review the budget in detail). The Saudi grants to Jordan ($300 million last year) will help but those grants should not be relied upon long-term.

¶6. (SBU) Abu Hammour was particularly concerned about the 25% increase in expenditures in this year's budget. Capital expenditures are welcome, he said, but can also add longer-term to an increase in current expenditures. The salary increases granted to civil servants pushed by Parliament and agreed to by the government will also cause a permanent increase in current expenditures.

¶7. (SBU) Abu Hammour fears that continued government over-spending could lead to a repeat of the dire economic conditions the country faced in the late 1980's, which culminated in Jordan being forced to devalue the dinar in ¶1989. Abu Hammour believes government over-spending over several years precipitated that crisis. Currently, government revenues are not keeping up with the rapid increase in expenditures. Abu Hammour believes not redressing this in the near future in risky.

¶8. (SBU) Abu Hammour noted that inflation last year was 6.25% and it is likely to moderate to 5% this year. However, this level is still higher than the base in previous years, which was in the 3% range. With inflation at these levels, economic orthodoxy would call for fiscal conservatism not the current expansionary fiscal policy.

¶9. (SBU) Finally, Abu Hammour is worried by the current

account deficit, at 20% of GDP. For the first time in years, he said, the current account is registering a deficit in both goods and services. To finance it, the government must either borrow more, thereby adding to the country's debt, or start to draw down on the over $5 billion in foreign reserves in government coffers. Neither approach would be sustainable for more than two or three years, he said.

COMMENT

¶10. (SBU) Abu Hammour was known as a technocratic Finance Minister and a fiscal conservative. He is certainly correct that continuation of the government's current fiscal policies is not sustainable over two or three more years. The twin deficits he identifies and government debt are indeed major challenges for the government. Nevertheless, Abu Hammour's pessimism is over-stated. The uptick in inflation last year was driven largely by the unprecedented surge in world oil prices. With the current moderation in those prices, inflation is moderating as well. Also, foreign reserves have continued to rise over the past several years.

¶11. (SBU) Jordan's middle and lower classes are still struggling with the continuing effects of the higher oil prices, the removal of government subsidies of fuel products, and a real estate boom, driven by foreign investment by Iraqis and the Gulf. This is driving up prices and making it harder for average Jordanians to buy homes. It is in this political context that the government agreed with Parliament to raise government salaries. Although this move has a clear fiscal impact, it was politically necessary, particularly in a year in which the country will be holding both Parliamentary and municipal elections. In addition, the privatization proceeds will be put to work offsetting some of Abu Hammour's concerns. Foreign direct investment continues to be positive and changes in tax policies should help moderate the revenue shortfall.
HALE